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COMPETITION · REGULATION · POLICY · STRATEGY

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Submission to the Economic Development, Science and Innovation Committee on the Commerce (Criminalisation of Cartels) Amendment Bill

Overview

1. This submission on the *Commerce (Criminalisation of Cartels) Amendment Bill* (**Bill**) is made by Matthews Law, a specialist competition law firm. As full-time specialists, advising on cartel issues is a core part of our practice, including advising clients on proposed collaborative arrangements and on Commerce Commission (**Commission**) investigations.[1] We have been involved in the consultation process on the proposal to criminalise cartel conduct since before the *Commerce (Cartels and Other Matters) Amendment Bill* (**Cartels Bill**) was introduced.

2. As the Committee knows, many of our peers specialising in competition law previously submitted against cartel criminalisation (**criminalisation**). We do not propose to relitigate those issues. However, we have concerns with a "pick up where we left off" approach to criminalisation, perhaps reflected in the Bill's drafting, which appears inconsistent.

3. In summary, we submit that:

    a. **Criminalisation should be considered in the current context**: Things have clearly moved on since 2011 when the Cartels Bill was introduced, including the enactment of new cartel laws in August 2017. The case for (and approach to) criminalisation should be considered in the context of the current law, including how that law is being interpreted and applied. The Regulatory Impact Statement (**RIS**) produced by the Ministry of Business, Innovation and Employment (**MBIE**) on 26 August 2011 should be revisited.

    b. **The "design" of the cartel regime risks criminalising benign behaviour**: The new cartel prohibition is broad and deliberately designed to overreach. In practice, most arrangements between actual or potential competitors risk being deemed "cartel provisions" as they are likely to relate to either price, capacity or output. While the new exceptions are clearly an improvement, they are still complex and impose a "reverse onus" on anyone seeking to rely on them. The complexities with the new law are compounded with criminalisation, and there is a real risk that this design will criminalise benign behaviour and that the exceptions may not be available.

    c. **The mental element should be clarified, and the defences reviewed**: It is not clear that simply overlaying a *mens rea* element of "intent" to the existing civil regime is appropriate. This approach should be clarified. The proposed defences should also be reviewed to ensure they are not overly narrow or unworkable.

    d. **Consideration should be given to the costs associated with the current law, and the potential for perverse settlement outcomes**: We urge the Committee to consider the real and significant costs associated with the current law (including compliance costs, investigation costs, and foregone opportunities), and how the prospect of criminal prosecution could impact parties' settlement incentives. Appropriate "checks and balances" should be built into the legislation.

[1] Principal Andrew Matthews has over 25 years' experience practicing in this area of the law, including 10 years as head of the Competition & Regulatory and TMT teams at trans-Tasman law firm Minter Ellison Rudd Watts. Andrew also practiced competition law at Allen & Overy in London, and Bell Gully in Auckland. He is actively involved in various international competition forums, including the International Bar Association, the Inter-Pacific Bar Association, and the American Bar Association, and has spoken at domestic and international conferences on cartel matters. Andrew has previously been a Non-Governmental Advisor at the International Competition Network.

4. We briefly expand on these points below. We are happy to appear in front of the Committee to discuss this submission.

Criminalisation needs to be considered in the current context

The RIS should be revisited

5. The Bill largely resuscitates provisions to criminalise cartel conduct that were originally proposed in the Cartels Bill, with some minor consequential changes. The Explanatory Note explains that the RIS, prepared by MBIE in 2011, helped inform the main policy decisions taken by the Government relating to the contents of *this* Bill. That was in the context of the Departmental Disclosure Statement (**DDS**) indicating that no amendments to the RIS were required.[2]

6. We submit that the RIS should be revisited. New Zealand's competition law environment has undergone considerable change since the RIS was produced around 7 years ago, and a fresh regulatory impact analysis is warranted. Among other things:

   a. The introduction of new cartel laws in August 2017 represent significant, complex changes to the Commerce Act 1986 (**Act**). The new (civil) cartel regime has proven more complex than anticipated, and we are encountering material differences in how lawyers, who are experienced in this area, are interpreting the new law. Policy decisions on criminalisation should be made in that context, not in the context of the "old law".

   b. As stated in the DDS, at the time the RIS was prepared the number of enforcement actions against domestic cartels was limited and since 2011, there have been at least four significant enforcement actions taken. That increase in enforcement action (and associated media) will have naturally raised businesses' awareness of cartel laws.

   c. It would appear inconsistent to adopt the RIS (as prepared in 2011) without reference to more recent documents relating to criminalisation, such as the Cabinet Committee Paper: Removal of the criminal offence for cartels from Commerce (Cartels and Matters) Amendment Bill (December 2015) and the subsequent Minute of Decision of the Cabinet Economic Growth and Infrastructure Committee, which stated that it was agreed to "*monitor domestic and international developments to better assess the potential effects of cartel criminalisation, and whether criminal sanctions for cartel conduct are desirable*".

Inconsistent drafting in the Bill may reflect the stop-start nature of this process

7. The changed context, and the stop-start nature of this process, appear to be reflected in some inconsistences in the drafting of the Bill. In particular, there appears to be a disjunct between what the Explanatory Note, DDS and Cabinet Paper state that the Bill will do, and how the Bill has been drafted. For example:

   a. The Explanatory Note and DDS both state that "*existing exceptions and exemptions in the Act to the civil prohibition for cartel conduct will also apply to the new criminal offence, including the exception relating to collaborative activities (such as joint ventures) and the exception for specified international shipping activities*" and the Cabinet Paper states "*the four exceptions in the Act that currently apply to civil prohibition would also be extended to apply to the new criminal offence. In particular, competitors that are involved in a collaborative activity or joint venture will not be subject to the criminal offence.*" However, competitors that are involved in a collaborative activity will still be *subject* to

[2] Section 2.3.2 of the DDS notes that there are "*a number of changes that are worth noting*", however it was considered that those changes did "*not materially impact on the analysis of the policy options in the RIS*."

the criminal offence (albeit they may claim that the collaborative activities exception applies), and it is also unclear why other exceptions to the cartel prohibition (eg the other exceptions in sections 43 and 44 of the Act) are not referred to in proposed section 82B(2).

b. The Explanatory Note and DDS both state that "*new defences in new section 82C… provide for circumstances where a defendant believes that the impugned conduct was reasonably necessary as provided for in one of the exceptions*" and the Cabinet Paper states "*given the seriousness of the criminal offence… an additional defence is proposed to recognise that a defendant could be factually mistaken about the availability of one or more of exceptions (new section 82C in the Bill).*" However, this is not reflected in the current drafting of the defences in section 82C, which do not include a defence for where a defendant believed that the exception for vertical supply contracts and/or exception for joint buying & promotion applied.

The "design" of the cartel regime risks criminalising benign behaviour

8. The new civil cartel prohibition is drafted to be deliberately broad. Even though it creates a "per se" prohibition, it deliberately errs on the side of capturing benign or competitively neutral conduct. If this approach applied to a criminal regime, this would create scope for conduct to be caught that does not fit into any accepted definition of "hard-core" cartel conduct. It is also conceivable that the exceptions/defences regime may not apply to such conduct.

9. For example, by following the (deliberate) overreach of the new civil cartel regime, the proposed criminal offence (as drafted) risks capturing neutral or even beneficial conduct such as:

   a. pubs in a university town agreeing to impose an earlier closing time to curb drunken behaviour (output restriction);

   b. competing supermarkets agreeing to not offer free plastic bags to customers to reduce waste (price fixing; output restriction);

   c. doctors agreeing to cap fees for the elderly (price fixing);

   d. car dealers agreeing not to sell cars with perceived safety issues (eg potentially faulty airbags) (output restriction).[3]

10. Arguably none of the examples above would fall within any of the available exceptions.

11. The Commission's (excellent) *Competitor Collaboration Guidelines* indicate that in order for there to be a "collaborative activity" (to benefit from the collaborative activities exception) there must be some form of "combination" of the business assets. Paragraph 105 states: *"It is the 'carrying on ... in cooperation' language that indicates that the parties must be combining their businesses, assets, or operations in some way in a commercial activity, or otherwise operating a commercial activity jointly".*

12. At a practical level, it is unlikely that parties seeking to undertake activities they see as having a clear "public good" will have turned their minds to the possibility of a cartel, let alone possible exceptions. Yet arguably they would have intended to do the "physical act".

[3] It is worth noting that many "cartel" provisions could fall with any one of the three prohibitions; conversely, it may be necessary to rely on one or more of the "exceptions" and that even this exercise may not be straightforward. It is also worth noting the difficulty for a party assessing whether there is in fact a "cartel" provision by virtue of the counterfactual test in section 30B.

The mental element should be clarified, and the defences reviewed

The mental element – "intent"

13. We refer to the submission dated 6 September 2012 by Andrew Matthews and Oliver Meech on the proposed criminalisation under the Cartels Bill (**Submission**).[4]

14. As stated in the Submission, the mental element for the criminal offence is at risk of being ambiguous and should be clarified. The Bill is intended to capture "hard core" cartel conduct as defined by the OECD. Proposed new section 82B provides that the mens rea is that the person "*intends, at that time, to engage in price fixing, restricting output or market allocating.*" Section 30A of the Act defines those terms separately in sub-sections (2)-(4).

15. Yet, as the above discussion should make clear, the intention to do the "physical act" of price-fixing, restricting output or market allocating (*as defined*) has the risk for significant overreach.

16. In January 2013, MBIE published its response to this concern (as raised in the Submission), which was simply "disagree" with no further explanation.

The defences

17. In addition to the potential for "overreach" it appears that the proposed new section 82C defences may be narrower than intended. For any of the exceptions or defences to apply, the defendant must have a relatively strong understanding of the Act in terms of what constitutes a cartel provision and the respective elements of each available exception. The proposed new section 82C defences require an assessment of whether the defendant believed the "offending" provision was "reasonably necessary" for the *collaborative activity*, necessitating that this analysis has taken place before the defences become available.

Consideration should be given to the costs associated with the current law, and the potential for perverse settlement outcomes

18. The costs and risks of litigation provide powerful incentives to settle through agreed facts and penalty. This can mean that all relevant factors are not fully known. It may not be fully appreciated that there are strong incentives on parties to settle cartel cases, even when they may have an arguable case.[5] Arguably this can be seen from the handful of defended cases (eg "*High Court sides with agencies that chose not to settle price-fixing case*").[6]

19. The incentive to settle (perhaps on a civil, rather than criminal, basis) could increase significantly with the introduction of a criminal offence, creating an increased risk of false positives. It may be prudent to consider having independent oversight of decisions made about issuing proceedings and prosecution in relation to cartels, and that such oversight is provided for legislatively.

20. Further consideration should be given to assessing whether the current regime is fit for purpose, and the costs (and benefits) of criminalising cartel conduct. We note:

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[4] A copy of the Submission is available at this link: https://www.parliament.nz/resource/en-NZ/50SCCO_EVI_00DBHOH_BILL11153_1_A275428/1af3a52aa3ff641be55a7f1c8516c3f78a2b9f0a

[5] We note that the comments on past enforcement actions in the DDS do not make it clear that, even under the old price fixing prohibition, most cartel cases were "settled" with agreed penalties. One of the cases was decided only under section 27. We do not recall having seen any discussion as to whether the prior regime led to "false positives".

[6] See: https://www.stuff.co.nz/business/98629666/high-court-sides-with-agencies-that-chose-not-to-settle-case.

a. New Zealand seems to have a highly effective leniency policy leading to prosecutions of domestic and international cartels. (There may even have already been a risk of "false positives" under the prior "price-fixing" prohibition.)

b. The Commission has both legislative and practical ways of sharing information with other regulators. In a cartel context, "waivers" to speak with other regulators are the "norm".

c. New Zealand has significant penalties both for companies and individuals and the maximum penalties have not been imposed to date.

d. Part 7 of the Act gives the Commission extremely powerful investigative tools, including the ability to conduct "dawn raids" and gather information using its compulsory information gathering powers. While there is an ostensible protection against self-incrimination, there is no right to silence.

e. The costs to business of complying with the new law and with Commission investigations are significant. Even the most straightforward investigation, which does not lead to any prosecution, can cost hundreds of thousands of dollars.

f. We are aware of potentially efficiency-enhancing and beneficial new collaborations not being pursued under the current regime due to the complexity of the new prohibition and exceptions. This could be expected to occur more often with criminalisation.

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